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RUEATRS/DEPT OF TREASURY WASHINGTON DC PRIORITY
RUEAWJA/DEPT OF JUSTICE WASHINGTON DC PRIORITY

C O N F I D E N T I A L SECTION 01 OF 02 VILNIUS 000459

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STATE FOR EUR/NB AND EB/ESC

E.O. 12958: DECL: 05/17/2016
TAGS: ENRG ECON EPET PREL PGOV ETRD NL RS LH
HT12, HT9
SUBJECT: POLISH COMPANY SURGING IN BID TO BUY LITHUANIAN REFINERY

REF: A. VILNIUS 349 AND PREVIOUS
¶B. 05 THE HAGUE 3119
¶C. JOHNSON/JONES E-MAILS 05/04/2006

Classified By: Economic Officer Scott Woodard for reason 1.4 b and d

¶1. (C) SUMMARY: The Polish energy company PKN Orlen has emerged as the frontrunner to secure a controlling interest in Lithuania's oil refinery, according to a reliable government source. Court challenges in the United States and Netherlands continue and may yet derail the sale of the refinery. END SUMMARY.

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YUKOS REACHES AGREEMENT WITH PKN ORLEN
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¶2. (C) Saulius Specius, an adviser to the Prime Minister and one of the GOL's lead negotiators on the sale of the Mazeikiu Nafta (MN) refinery, told us on May 17 that the sale of MN had taken a new twist in favor of the Polish energy company PKN Orlen (PKN). He said that Yukos had reached an agreement to sell its 53.7 percent of MN shares directly to PKN. The GOL, he said, had reached an agreement in principle to sell all (or almost all) of its 40.6 percent ownership of MN to PKN as well. PKN would buy a 30 percent stake in MN from the GOL, with an option to purchase the rest of the GOL's shares within five years. Specius added that Lithuanian law currently requires the GOL to own at least 10 percent of MN's shares, a requirement that parliament will need to amend to allow PKN to exercise this option.

¶3. (U) Press reports from mid-April, citing unofficial PKN sources, suggested that PKN was prepared to pay approximately USD 2.5 billion for the shares held by Yukos and the GOL: USD 1.5 billion for Yukos's entire stake and USD 1 billion for all of the GOL's shares. Specius noted that this deal would turn the GOL shares to cash and eliminate the government's risk of getting stuck with a frozen asset or a minority share of limited interest to other buyers.

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SITTING HERE IN LEGAL LIMBO
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¶4. (C) Meanwhile, the GOL awaits the outcome of the May 19 New York Bankruptcy Court hearing of the case that Yukos receiver Eduard Rebgun filed on behalf of Yukos creditors (ref C). Specius said that Yukos's executives hope to use PKN's signature on the purchase agreement as evidence that

the MN sale will benefit Yukos's creditors -- evidence that might persuade the judge to lift the temporary restraining order that bars Yukos from executing the MN sale.

¶5. (C) Specius expects there will also be a hearing in the Dutch courts May 18 on the bankruptcy case involving Yukos International UK BV, the Dutch legal entity that owns the majority stake in MN. He said it is unclear, however, whether the May 18 hearing involves the case Rebgun filed in the Netherlands in April or a case Yukansneftegaz filed earlier (ref B). He also said that it was not yet clear how this case (or these cases) might affect MN's sale.

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EXPENSIVE OIL INCREASES MN'S OPTIONS
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¶6. (C) Specius told us that the current high price of crude and refined petroleum products means that MN's profitability no longer depends solely on Russian supply or transport of crude. He acknowledged that MN will be most profitable if it receives Ural crude via pipeline, but will turn a profit even if Russia turns off the spigot and MN has to bring crude in through its Baltic Sea terminal at Butinge. This profit point, Specius said, allowed the GOL to consider companies like PKN-Orlen and Kazmunaygaz as competitors to their Russian rivals like TNK-BP and Lukoil.

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COMMENT
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¶7. (C) Specius is a well-placed source, but we suspect that



this is not the final chapter in the struggle for control over the refinery. Litigation relevant to the sale continues in several foreign jurisdictions. In Lithuania, the intrigue and infighting between many interests over the company's largest private enterprise persist.

¶8. (C) PKN's apparent emergence as the frontrunner is certainly newsworthy, however. It has been in the running as a potential buyer for the past several months, but few people gave it a chance, noting that it seemed less capable of providing a guaranteed supply of crude than other bidders (KazMunayGaz, TKN-BP, and Lukoil). The high price of both crude and refined products, however, may have changed the calculations. The big surprise here is the GOL's apparent interest in getting out of the oil business, which it has regarded since independence as strategic. One possible explanation is that, as soon as the plant is operating, the government will reap its tax revenues, without the risk of holding onto a minority interest of no cash value.
KELLY